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No. 06-989

IN THE

Supreme Court of the United States

HALL STREET ASSOCIATES, L.L.C.,
Petitioner,

v.

MATTEL, INC.,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

REPLY BRIEF OF PETITIONER

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RULE 29.6 CORPORATE DISCLOSURE STATEMENT

The Rule 29.6 Corporate Disclosure Statement in the petition for writ of certiorari and incorporated in the opening brief remains correct.

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REPLY BRIEF OF PETITIONER

INTRODUCTION

The Federal Arbitration Act's ("FAA") primary purpose is "ensuring that private arbitration agreements are enforced according to their terms." *Volt Info. Sciences, Inc. v. Board of Trs. of Leland Stanford Junior Univ.*, 489 U.S. 468, 479 (1989); *see also Dean Witter Reynolds Inc. v. Byrd*, 470 U.S. 213, 220 (1985). Because arbitration under the FAA is a matter of contract, the FAA allows "the enforcement of agreements to arbitrate under different rules than those set forth in the Act itself." *Volt Info. Sciences*, 489 U.S. at 479. Consistent with those precepts, the FAA does not prohibit enforcement of private arbitration agreements in which the parties agree to judicial review of an arbitration award for legal error.

Petitioner Hall Street Associates ("Hall Street") and respondent Mattel, Inc. ("Mattel") voluntarily entered into an agreement explicitly preserving legal error as a ground for judicial vacatur of the arbitration award. Having made that bargain, Mattel now seeks to avoid it, arguing that the FAA does not list legal error as a ground for vacatur. Mattel's argument fails because the FAA's statutory grounds for vacatur are not exclusive.

The FAA does not preempt or forbid agreements which restrict the submission to the arbitrator and reserve final authority over legal issues to the court. To the contrary, the FAA ensures private parties' freedom to contract for arbitration provisions – including legal-error review provisions – which are tailored to their individual dispute resolution needs. *See Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 57 (1995) ("the FAA's proarbitration policy does not operate without regard to the wishes of the contracting parties"); *Dean Witter Reynolds*, 470 U.S. at 221 (courts must "rigorously enforce agreements to arbitrate" according to their terms).

Mattel's statement of the case is a distraction, calculated to imply that the district court erred in concluding that the award contains legal error.[1] Resp. Br. 11. But even the reviewing

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[1] Although Mattel claims that the district court vacated the arbitration award "based on its view that there were errors of fact and law underlying the award," Resp. Br. 1, the district court reviewed only claims of legal error. Pet. App. 51a-56a. Mattel also insinuates that the district court's review of the arbitration award was irregular because Hall Street did not provide the full arbitration record to the court. Resp. Br. 11. Each party, however, directed the court to those parts of the record that they deemed relevant. Jt. App. 4-5 (Dt. Ct. Dkt. Nos. 71 (February 13, 2002); 73 (February 25, 2002); 77 (March 8, 2002)). The complete arbitration record was lodged with the court well before its second opinion vacating the award. Jt. App. 10-12 (Dt. Ct. Dkt. Nos. 130-131, 144 (July 15, 2003); 135-137 (July 30, 2003); 138 (August 11, 2003); 139-141, 145 (August 18, 2003)).

court below acknowledged that "the arbitrator's assessment of the merits in this case contains possible errors of law[.]" Jt. App. 156. The dissenting judge concluded that "the arbitrator's decision was completely irrational." *Id.* at 157.

Ultimately, however, the correctness of the arbitrator's decision is beside the point. The only question before this Court is whether the FAA prohibits parties from limiting the submission to the arbitrator and agreeing that a court may vacate the arbitration award for legal error. Because nothing in the FAA – or any other law – prohibits such agreements, the parties' arbitration agreement should be enforced.

ARGUMENT

I. THE FAA DOES NOT FORBID PARTIES FROM AGREEING THAT AN ARBITRATION AWARD WILL BE VACATED FOR LEGAL ERROR.

Mattel wrongly suggests that Hall Street must show that the FAA affirmatively authorizes arbitration agreements providing for legal-error review. *See, e.g.*, Resp. Br. 16. In fact, it is Mattel's burden to show that the FAA affirmatively prohibits arbitration agreements preserving judicial authority to review for legal error, or that such agreements otherwise are unenforceable as a matter of law. *See Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24-25 (1983) (section 2 of the FAA establishes a presumption in favor of the enforceability of private arbitration agreements according to their terms); *see also Muschany v. United States*, 324 U.S. 49, 66 (1945) ("As the term 'public policy' is vague, there must be found definite indications in the law of the sovereignty to justify the invalidation of a contract as contrary to that policy."); *Baltimore & Ohio Sw. Ry. Co. v. Voigt*, 176 U.S. 498, 505 (1900) ("the usual and most important function of courts of justice is rather to maintain and enforce contracts, than to enable parties thereto to escape from their

obligation on the pretext of public policy, unless it clearly appear that they contravene public right or the public welfare"). Mattel cannot make that showing.

A. The FAA Did Not Withdraw the Courts' Traditional Authority to Vacate Arbitral Awards for Legal Error Based on the Contracting Parties' Agreement.

Prior to the adoption of modern arbitration statutes, courts long had exercised their authority to review and vacate arbitral awards for legal error when parties provided for the application of legal rules in their arbitration agreements or clearly stated their intent to restrict the submission to the arbitrator. As Justice Story explained in *Kleine v. Catara*, 14 F. Cas. 732, 735 (C.C.D. Mass. 1814):

> If the parties wish to reserve the law for the decision of the court, they may stipulate to that effect in the submission; they may restrain or enlarge its operation as they please. If no such reservation is made in the submission, the parties are presumed to agree, that every thing, both as to law and fact, which is necessary to the ultimate decision, is included in the authority of the referees.

See also Fudickar v. Guardian Mut. Life Ins. Co., 62 N.Y. 392, 401 (1875) ("If it appear[s] from the award that the arbitrators intended to decide the case according to the law, and the grounds for their decision are set out, which in law do not justify it, the case is brought within the exception to the general rule, and the court will set it aside."); *Greenough v. Rolfe*, 4 N.H. 357, 359 (1828) (same).

Mattel does not dispute that courts traditionally possessed authority to review and vacate arbitral awards for legal error when specified by agreement. According to Mattel, however, § 9 of the FAA is a "patently clear" expression of congressional intent to divest courts of authority to vacate arbitral awards for legal error, even when parties expressly and

unambiguously preserve legal error as a ground for vacatur in their agreement. Resp. Br. 21. Mattel's argument focuses on only a select portion of the text of § 9 and ignores the qualifying text that precedes it.

Section 9 requires a court to enter an order confirming an arbitration award *only* "[i]f the parties in their agreement have agreed that a judgment of the court shall be entered upon the award made pursuant to the arbitration[.]" 9 U.S.C. § 9. The text of § 9 expresses Congress's intent that a court must enforce the agreement of the parties as to whether, and under what circumstances, a judgment shall be entered on an award. In so providing, § 9 necessarily allows parties to define and limit the scope of the arbitration and the arbitrator's power. Here, the parties plainly did not "agree[] that a judgment of the court shall be entered upon the award" unless and until the court decided that the award did not contain legal error. 9 U.S.C. § 9.

This point is driven home by § 2 of the Act, which makes clear that parties' agreements – including agreements specifying supplemental grounds for vacatur – are paramount when the agreements otherwise are enforceable under contract law. *See* 9 U.S.C. § 2 (arbitration agreements "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract"). Section 2 establishes a "broad principle of enforceability" of arbitration agreements according to their terms. *Southland Corp. v. Keating*, 465 U.S. 1, 11 (1984). Mattel's restrictive interpretation of § 9 would place that provision of the FAA in needless tension with § 2 and the FAA's statutory policy of "unobstructed enforcement of arbitration agreements." *See Moses H. Cone Mem'l Hosp.*, 460 U.S. at 23; *see also Cortez Byrd Chips, Inc. v. Bill Harbert Constr. Co.*, 529 U.S. 193, 200-01 (2000) (refusing to endorse restrictive reading of the venue provisions in §§ 9 to 11 of the FAA, in part because

such a reading could deprive the parties of the forum previously selected by agreement of the parties). Section 9 should not be interpreted to invalidate agreements concerning the prerequisites for a binding arbitration award. Parties who agree to judicial review for legal error agree to be bound by an arbitration award *only* if the court confirms that the award contains no legal error.[2]

Contrary to Mattel's claim, interpreting § 9 to allow parties to specify legal error as a ground for vacatur of arbitration awards does not deprive § 9's references to §§ 10 and 11 of meaning. Parties generally accept the limited grounds for vacatur or modification of arbitration awards under the FAA and common law. *See* Margaret Moses, *Can Parties Tell Courts What to Do? Expanded Judicial Review of Arbitral Awards*, 52 KAN. L. REV. 429, 443 (2004). In those cases, §§ 10 and 11 – and the common-law exceptions – provide the sole grounds on which a court may decline to enforce an award.

Sections 10 and 11 apply even when parties specify additional grounds for vacatur or modification of arbitration agreements. In those cases, §§ 10 and 11 establish a default rule which parties may agree to supplement with additional grounds for vacatur, so long as those additional grounds are consistent with normal judicial functions and otherwise enforceable as a matter of contract law.

Mattel also contends that an arbitration agreement preserving judicial authority to review for legal error is not an

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[2] This reading of the FAA is strongly supported by the fact that "absent an affirmative indication of Congress' intent to preclude waiver, [this Court has] presumed that statutory provisions are subject to waiver by voluntary agreement of the parties." *United States v. Mezzanatto*, 513 U.S. 196, 201 (1995). Mattel's position necessarily is that the right to confirmation of an award with legal errors cannot be waived, no matter how clear and unmistakable that waiver is. Nothing in the FAA suggests that the parties here could not waive any alleged statutory right to confirmation of an award containing legal errors; in light of the FAA's focus on enforcement of the parties' agreement, the opposite is true.

arbitration agreement within the meaning of § 2 because it does not "settle" the controversy. Resp. Br. 25. Mattel's argument proves too much. Under Mattel's logic, such an arbitration agreement is not even subject to the FAA because, according to Mattel, judicial-review provisions prevent the agreement from constituting an agreement to "settle" the parties' dispute by arbitration. If this is true, any statutory limits on judicial review of the arbitration award would not apply in any event.

Mattel's contention that legal-error review provisions deprive arbitrators of authority to "settle" disputes is also incorrect. Parties who enter arbitration agreements containing such provisions simply limit the scope of their submission to the arbitrator and preserve the court's authority to review an award for legal error. If no party contests the award or if the court finds neither legal error nor any statutory or common-law ground for vacatur, the award "settles" the dispute.

Finally, Mattel argues that § 10 prescribes the exclusive grounds for vacatur of an award because certain sections of the FAA expressly apply only in the absence of a contrary agreement by the parties. Resp. Br. 22; *see also, e.g.*, 9 U.S.C. § 5 (providing the method for selecting an arbitrator if "no method be provided" in the parties' agreement). This Court's decisions demonstrate that Mattel's interpretation of the FAA is wrong. This Court repeatedly has recognized that provisions of the FAA which contain no reference to the parties' agreement nonetheless may be varied by mutual consent. In *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 943 (1995), for example, this Court made clear that parties may agree that the question of arbitrability will be decided by the arbitrator, rather than by the courts, even though § 3 of the FAA assigns the task of determining whether an issue is "referable to arbitration" to the courts,

without any express reservation of the parties' right to agree otherwise.

Similarly, in *Volt Info. Sciences*, the parties' contract specified that disputes would be governed by California law. Volt sought to compel arbitration under the FAA, while its opponent, Stanford, sought to stay the arbitration pending the outcome of related litigation under California law. 489 U.S. at 470-71. This Court recognized that the FAA contained no provision authorizing a stay of arbitration pending litigation or allowing the parties to agree to such a provision. *Id.* at 476-77. The Court nonetheless affirmed the state court's enforcement of the parties' agreement to apply California law on the stay question, stating: "There is no federal policy favoring arbitration under a certain set of procedural rules; the federal policy is simply to ensure the enforceability, according to their terms, of private agreements to arbitrate." *Id.* at 476. *See also Southland*, 465 U.S. at 18 (Stevens, J., concurring in part and dissenting in part) ("the *limited objective* of the [FAA] was to abrogate the general common-law rule against specific enforcement of arbitration agreements" (emphasis added)).

Mattel's proffered reading of §§ 9 and 2 would give binding effect to arbitration awards which *violate* the parties' express agreements. Although the FAA promotes the enforceability of arbitration agreements, this Court has cautioned that "the FAA does not require parties to arbitrate when they have not agreed to do so[.]" *Volt Info. Sciences*, 489 U.S. at 478. Parties who agree to judicial review for legal error expressly have declined to accept the arbitrator's legal rulings as final; instead, they have agreed to be bound by an arbitration award *only* if the court confirms that the award contains no legal error. Nothing in the FAA evinces a congressional intent to forbid courts from reviewing arbitral awards for legal error where, as here, the parties unambiguously agreed to that review.

B. This Court's Decisions Confirm that the Statutory Grounds for Vacatur or Modification of Arbitration Awards Are Not Exclusive.

In arguing that § 10 sets forth the exclusive grounds for vacatur of arbitration awards despite the parties' agreement to judicial review for legal error, Mattel attempts to distinguish this Court's decisions establishing that the FAA's grounds for vacatur and modification of arbitration awards are not exclusive. Mattel's arguments are unpersuasive.

Mattel claims that this Court has not recognized any grounds for the vacatur or modification of arbitration awards other than those in §§ 10 and 11. Resp. Br. 23. Faced with *Wilko v. Swan*, 346 U.S. 427 (1953), *overruled on other grounds by Rodriquez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989), Mattel argues that "manifest disregard" of the law either is not a ground for vacatur at all or is encompassed within § 10.

Wilko cannot be so easily distinguished. First, this Court subsequently has referred to "manifest disregard" as a non-statutory ground for vacatur. *See First Options*, 514 U.S. at 942 (listing "manifest disregard of the law" as additional to the grounds for vacatur listed under § 10 and noting that *Wilko* had been "overruled on other grounds"); *Shearson/American Express Inc. v. McMahon*, 482 U.S. 220, 259 (1987) (Blackmun, J., concurring in part and dissenting in part) (describing judicial review under the FAA as normally limited to "the four grounds listed in § 10 of the [FAA] *and* to the concept of 'manifest disregard' of the law" (emphasis added)). Most lower courts also correctly recognize "manifest disregard of the law" as a "non-statutory" ground for vacatur of arbitration awards. *See, e.g., McCarthy v. Citigroup Global Mkts., Inc.*, 463 F.3d 87, 91 n.6 (1st Cir. 2006) ("Nowhere in 9 U.S.C. § 10 does the phrase 'manifest disregard of the law' appear."); *Hoeft v. MVL Group, Inc.*, 343 F.3d 57, 65 (2d Cir. 2003) (describing "manifest disregard of the law" as

a common-law ground for review); *Prestige Ford v. Ford Dealer Computer Servs.*, 324 F.3d 391, 396 (5th Cir. 2003) (same); *Scott v. Prudential Sec. Inc.*, 141 F.3d 1007, 1017 (11th Cir. 1998) (same).

Mattel's dismissal of *W.R. Grace Co. v. Local Union 759*, 461 U.S. 757 (1983), is similarly unconvincing. Although *W.R. Grace* involved arbitration under a collective bargaining agreement, this Court's reasoning was not limited to that context. Indeed, this Court expressly stated that the public policy exception applied to "any contract." *Id.* at 766. No reason exists for arbitration agreements under the FAA to be exempt from that rule. *See Circuit City Stores, Inc. v. Adams*, 532 U.S. 105 (2001) (FAA covers most employment contracts).[3]

In sum, the FAA does not establish the exclusive grounds for vacatur of awards even under federal law, and it certainly does not preempt the parties' right to contract for different arbitration rules and proceedings. Indeed, *Volt Info. Sciences* makes clear that the FAA does nothing to limit parties' ability to shape their arbitration agreements as they see fit, even if they voluntarily invoke the law of another sovereign. *See* 489 U.S. at 479 (parties may limit scope of arbitration agreements and structure as they see fit). Although Mattel argues that allowing parties to contract for legal-error review provisions would permit parties "to be [their] own sovereign[s,]" Mattel identifies no reason – nor is any apparent – why parties should be limited to adopting state arbitration laws. The

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[3] The courts of appeals routinely apply the "public policy" ground for vacatur to FAA cases. *See, e.g., Lessin v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 481 F.3d 813, 816 (D.C. Cir. 2007) (describing manifest disregard and public policy exceptions as additional to statutory grounds for judicial review under FAA); *B.L. Harbert Int'l, LLC v. Hercules Steel Co.*, 441 F.3d 905, 910 (11th Cir. 2006) (arbitrary and capricious, manifest disregard of the law, and public policy grounds for vacatur supplement the FAA's statutory grounds for vacatur).

FAA's paramount policy and purpose is the enforcement of parties' agreements to arbitrate according to the parties' terms. *See, e.g., Mastrobuono*, 514 U.S. at 53-54. Nothing in the FAA or any preemption doctrine precludes parties from setting their own contract terms. *Cf. American Airlines, Inc. v. Wolens*, 513 U.S. 219, 221 (1995) (holding federal law preempting state regulation nonetheless "allows room for court enforcement of contract terms set by the parties themselves").

C. The Legislative History of the FAA Confirms that the FAA's Primary Goal Is Enforcement of Private Agreements to Arbitrate.

According to Mattel, the FAA's legislative history "reflects a deliberate choice by Congress to reject the alternative approach of some of the contemporaneous arbitration laws that permitted vacatur of arbitration awards for legal error." Resp. Br. 27. An examination of that legislative history reveals no support for Mattel's contention.

The FAA's purpose was "to reverse the longstanding judicial hostility to arbitration agreements that had existed at English common law and had been adopted by American courts, and to place arbitration agreements upon the same footing as other contracts." *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 24 (1991); *see also* IAN R. MACNEIL, AMERICAN ARBITRATION LAW – REFORMATION, NATIONALIZATION, INTERNATIONALIZATION, at 15 (1992) ("AMERICAN ARBITRATION LAW") (the primary goal of FAA proponents was making arbitration agreements enforceable and irrevocable). Prior to the FAA's enactment, arbitration agreements commonly were revocable at any time prior to the issuance of an award. MACNEIL, AMERICAN ARBITRATION LAW, at 20. The FAA's proponents were focused on making arbitration agreements fully enforceable and irrevocable – not

on the grounds for vacatur.[4] *See, e.g., Arbitration of Interstate Commercial Disputes: Joint Hearings on S. 1005 and H.R. 646 before the Senate and House Subcomm. of the Comms. on the Judiciary*, 68th Cong., at 7 (1924) ("*1924 Hearings*") (testimony of Charles L. Bernheimer, urging the FAA's adoption so that "the parties cannot, as they can in most of our States and certainly in connection with interstate business, back out at the last moment when they see the case is going against them.").

Mattel suggests that Congress deliberately divested courts of authority to review arbitration awards for legal error by rejecting Illinois's arbitration statute and, instead, modeling the FAA after the New York Arbitration Act of 1920. Resp. Br. 27. A review of the legislative history reflects no such deliberation. The FAA was drafted by the American Bar Association and was the sole proposal presented to Congress. MACNEIL, AMERICAN ARBITRATION LAW, at 92. At *no* point in the congressional hearings did any person mention – much less argue against – the Illinois Arbitration Act of 1917 or its standards of judicial review.[5] Instead, proponents presented

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[4] Mattel's reliance on the statements of ABA delegates ignores this Court's admonition that the Court "ought not attribute to Congress an official purpose based on the motives of a particular group that lobbied for or against a certain proposal - even assuming the precise intent of the group can be determined[.]" *Circuit City Stores*, 532 U.S. at 120. Mattel also relies on statements by ABA delegates which were not even made to Congress, but rather to the National Conference of Commissioners on Uniform State Laws. *See, e.g.*, Resp. Br. 29.

[5] Notably, the Illinois Act did not address consensual agreements to permit review for legal error. Instead, it endorsed an approach whereby either party could seek a judicial determination of *any* legal questions that arose during the arbitration, and the arbitrator would be compelled to follow the court's legal decision. *See* Laws of Ill. 1917, ch. 202, § 6(a). Thus, even if Congress deliberately had rejected the Illinois Act – which it did not – that would not reveal a congressional intent to prohibit agreements allowing courts to vacate arbitral awards for errors of law.

the FAA to Congress as the only approach to arbitration with "no open opposition anywhere." *1924 Hearings*, at 13 (testimony of Julius Cohen).

Nor is there any evidence in the FAA or its history that Congress intended to deprive courts of preexisting authority to review arbitral awards for legal error when parties stipulate to such review in their arbitration agreements. *See* 65 CONG. REC. 1931 (1924) (testimony of Rep. Graham, stating: "[the FAA] does not involve any new principle of law except to provide a simple method by which parties may be brought before the court in order to give enforcement to that which they have already agreed to. . . . It does nothing more than that."). Certainly, the assertion that the FAA is modeled after the 1920 New York Arbitration Act does not assist Mattel because the New York statute did not prohibit legal-error review provisions.

The availability of judicial review for legal error traditionally depended on the parties' arbitration agreement. *See* James M. Gaitis, *Unraveling the Mystery of Wilko v. Swan: American Arbitration Vacatur Law and the Accidental Demise of Party Autonomy*, 7 PEPP. DISP. RESOL. L.J. 1, 17 (2007) ("From its earliest beginnings, the foundation of American arbitration law always has been the fundamental principle that it is the parties' 'submission' that determines the scope of the arbitrators' authority and, in consequence, the power of courts to vacate arbitral awards."). If the parties did not reserve the court's authority to review the arbitral award, courts interpreted their agreements to give final authority to the arbitrator on issues of both law and fact. *See, e.g.*, *Kleine*, 14 F. Cas. at 735. But if the parties stipulated that a court would review an award for legal error, the courts honored those agreements. *Id.*

New York applied that same rule. Although review for legal error was generally unavailable under New York law, New York courts reviewed arbitral awards for legal error

when the parties' contract contemplated such review. *See Fudickar*, 62 N.Y. at 400 ("[An arbitration award] may also be set aside for error of law, when the question of law is stated on the face of the award, and it appears that the arbitrators meant to decide according to the law but did not."). Although that common-law authority predated the 1920 New York Arbitration Act, contemporaneous commentators did not view the statute as restricting judicial authority to review for legal error. *See* Philip G. Phillips, *Rules of Law or Laissez-Faire in Commercial Arbitration*, 47 HARV. L. REV. 590, 603 (1933-34) ("In all states, if the parties provide in their arbitration agreement that the arbitrators must decide according to law, the courts will hold the arbitrators to that agreement and will review their law on appeal"); WESLEY A. STURGES, A TREATISE ON COMMERCIAL ARBITRATION AND AWARDS, at 500, 503 (1930) ("under an unrestricted submission arbitrators are not required to decide 'according to law'" but "if it is made to appear that the arbitrators undertook to decide according to law but missed it," the court may vacate award). Thus, Mattel's claim that Congress intentionally modeled the FAA after the New York statute does not prove any congressional intent to divest courts of their authority to review arbitration awards for legal error when parties expressly agree that legal error is a ground for vacatur.

II. THE PARTIES' AGREEMENT TO LIMITED ARBITRATION IS FULLY ENFORCEABLE AND DOES NOT INTERFERE WITH JUDICIAL FUNCTIONING AND INTEGRITY.

In the absence of barriers to legal-error review provisions under the FAA, the question becomes whether agreements containing such provisions are unenforceable on any other ground. Neither Mattel nor its *amici* identify any defenses which would render legal-error review provisions unenforceable as a matter of contract law. Instead, they argue that allowing parties to agree to legal error as a ground for vacatur

would interfere with judicial functioning and raise questions of "constitutional doubt." Resp. Br. 36-41; American Arbitration Association ("AAA") Br. 20-21. Neither argument has merit.

As an initial matter, unlike the agreements at issue in *Swift & Co. v. Hocking Valley Ry. Co.*, 243 U.S. 281 (1917), and *Estate of Sanford v. Commissioner of Internal Revenue*, 308 U.S. 39 (1939), agreements identifying legal error as an additional ground for vacatur do not tell courts what law to apply in deciding whether to vacate an arbitration award. Such agreements simply identify legal error in an arbitral award as nonbinding and subject to judicial review. Identifying legal error as an issue preserved for judicial review does not tell courts what degree of deference the court must afford to the arbitrator in undertaking that review. *See* Ronald R. Hofer, *Standards of Review – Looking Beyond the Labels*, 74 MARQ. L. REV. 231, 233 (1991) ("Standards of review classically include two elements: An identification of the type of issue, and the measure of deference paid to that issue"). Instead, as argued in Hall Street's opening brief, courts will review the arbitrator's award with the degree of deference that is consistent with the court's normal judicial functions. Because courts generally apply *de novo* review to claims of legal error, for example, that standard presumably will apply when courts review arbitral awards for legal error.

An agreement preserving legal error as a ground for vacatur neither confers new authority on federal courts nor dictates their functions. Parties to such agreements merely add a contractual ground for vacatur to the statutory grounds for review under the FAA, reinstating their rights to have courts act as the final decision-maker on issues of law. *See* Stephen J. Ware, *Punitive Damages in Arbitration: Contracting Out of Government's Role in Punishment and Federal Preemption of State Law*, 63 FORDHAM L. REV. 529, 542 n.50 (1994) ("parties to [arbitration agreements providing for judicial review for legal error] have contractually

reinstated their substantive rights, which otherwise would have been contractually waived by agreeing to arbitrate").

The constitutional arguments of Mattel and its *amici* fail because they are predicated on the erroneous assumptions that legal-error review provisions dictate court functions and allow parties to stipulate to law. *Amicus* AAA, for example, argues that allowing parties to preserve legal error as a ground for vacatur impermissibly delegates Congress's "power to make law to private parties." AAA Br. 20. As discussed above, however, such contracts neither "make law" nor delegate congressional authority to private parties. Instead, in contracting for legal-error review of arbitration awards, parties agree to preserve the authority of the courts to determine issues of law in cases under their jurisdiction.

Mattel argues that interpreting the FAA to permit parties to contract for legal-error review "raises serious constitutional doubt under Article III" because arbitrators are not subject to the control of Article III judges. Resp. Br. 40. No decision of this Court suggests that Article III judges must supervise arbitrators in order to review their decisions, much less supports a claim that such review raises grave constitutional doubt sufficient to trigger the avoidance doctrine. In *Peretz v. United States*, 501 U.S. 923 (1991), this Court rejected an argument that the use of a magistrate to preside at jury selection constituted a "congressional attempt to transfer jurisdiction [to non-Article III tribunals] for the purpose of emasculating constitutional courts[.]" *Id.* at 937 (internal quotations and citations omitted). Such separation-of-powers concerns are not implicated by private arbitration agreements allowing legal-error review, particularly where, as here, the parties entered into the agreement in the middle of litigation, and the district court expressly approved the agreement. Moreover, if such agreements raise constitutional doubts, the same doubts would apply to administrative law proceedings and all private methods of dispute resolution not subject to the direct control of Article III judges.

III. ENFORCEMENT OF ARBITRATION AGREEMENTS PRESERVING JUDICIAL AUTHORITY TO REVIEW FOR LEGAL ERROR PROMOTES THE GOALS OF THE FAA AND ENCOURAGES ARBITRATION.

Mattel and its *amici* argue that allowing the parties the freedom to contract for legal-error review will burden courts, undermine the arbitral process, and make the United States a less attractive forum for international arbitration. None of these policy arguments has empirical support or otherwise justifies singling out arbitration contracts as unenforceable. Moreover, contrary to Mattel's and its *amici*'s claims, enforcement of arbitration agreements preserving judicial authority to review for legal error promotes the goals of the FAA and encourages arbitration.

Amicus AAA first complains that allowing legal-error review provisions will make arbitrators "likely to demand more formalized evidentiary procedures and findings of fact, and feel compelled to create a record and a reasoned decision which will withstand court review." AAA Br. 9-10. AAA misses the point. The FAA permits parties to fashion their agreements to promote greater predictability and adherence to the law.

Although arbitration historically was a method of dispute resolution that relied on industry customs and other nonlegal considerations to guide decision-making, it increasingly has become a forum for adjudicating legal rights. Sarah Rudolph Cole, *Managerial Litigants? The Overlooked Problem of Party Autonomy in Dispute Resolution*, 51 HASTINGS L.J. 1199, 1241 (2000). This Court's decisions allowing statutory claims to be subject to arbitration are premised on the very requirement that arbitrators must follow the law. *See id.*; *see also Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 638 (1985) ("Having permitted the arbitration to go forward, the national courts of the United States

will have the opportunity at the award-enforcement stage to ensure that the legitimate interest in the enforcement of the anti-trust laws has been addressed."). As this Court has recognized, parties to arbitration agreements "do not forgo [their] substantive rights" and, instead, only submit the resolution of their dispute to "an arbitral, rather than judicial, forum." *Gilmer*, 500 U.S. at 26 (internal citation and quotation marks omitted).

Arbitrators, however, do not always feel bound to apply the law. According to one study, 90 percent of commercial arbitrators report a belief that they are free to ignore the law "whenever they thought that more just decisions would be reached by doing so." Stephen J. Ware, *Default Rules from Mandatory Rules: Privatizing Law Through Arbitration*, 83 MINN. L. REV. 703, 719-20 (1999) (internal quotation marks and citations omitted). Allowing parties to contract for legal-error review of arbitral awards is one way to protect the "important social policies" embodied in certain statutory rights, while still conserving judicial resources by promoting arbitration. *See Gilmer*, 500 U.S. at 27; *see also* Ware, 83 MINN. L. REV. at 734-35 (arguing same). The fact that legal-error review provisions may encourage arbitrators to apply the law carefully is a consideration weighing in favor of – not against – enforcing such provisions.

Mattel's and its *amici*'s arguments concerning alleged burdens on courts are similarly unpersuasive. *See, e.g.*, AAA Br. 6-12. For example, although the Fifth Circuit has permitted expanded judicial review provisions since 1995, Hall Street has been able to identify only three written district court decisions from that circuit in which a court applied such a provision in reviewing an arbitration award.[6] Even courts

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[6] *SFX Motor Sports, Inc.* v. *Chris Agajanian Presents, Inc.*, Case No. H-04-0601, 2006 U.S. Dist. LEXIS 1427 (S.D. Tex. Jan. 10, 2006); *Spinal Concepts, Inc.* v. *Curasan*, Case No. 3:06-CV-0448-P, 2006 U.S. Dist. LEXIS 63987 (N.D. Tex. Sept. 7, 2006); *Hughes Training, Inc.* v. *Cook*,

prohibiting expanded judicial review recognize that such review is less burdensome than plenary adjudications on the merits. *See, e.g.*, *Bowen* v. *Amoco Pipeline Co.*, 254 F.3d 925, 936 n.6 (10th Cir. 2001). As Judge Kozinski observed in his concurrence approving judicial-review provisions, "enforcing the arbitration agreement – even with enhanced judicial review – will consume far fewer judicial resources than if the case were given plenary adjudication." *Lapine Tech. Corp.* v. *Kyocera Corp.*, 130 F.3d 884, 891 (9th Cir. 1997) (Kozinski, J., concurring), *vacated sub nom. Kyocera Corp. v. Prudential-Bache T Servs., Inc.*, 341 F.3d 987 (9th Cir. 2003) (en banc), *petition for cert. dismissed*, 124 S. Ct. 980 (2004). And, as Hall Street already has explained, legal-error review provisions are consistent with courts' normal judicial functions, requiring courts to undertake the same type of review that they regularly conduct in a variety of contexts. *See id.* (Kozinski, J., concurring) ("The review to which the parties have agreed is no different from that performed by the district courts in appeals from administrative agencies and bankruptcy courts, or on habeas corpus.").

Concerns about legal-error review provisions undermining the efficiency of arbitration are misplaced. Arbitration promotes efficient dispute resolution only if parties are willing to use it. If the FAA is interpreted inflexibly to prohibit legal-error review provisions, parties who value legal certainty and adherence to legal principles in the decision-making process will simply choose to litigate their disputes in court. Allowing parties the flexibility to include legal-error review provisions in their arbitration agreements will reduce the burden on the judiciary by encouraging arbitration, particularly in complex commercial disputes. Furthermore, even assuming that judicial review for legal error may, on occasion, reduce some of the efficiencies associated with arbitration, this Court

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148 F. Supp. 2d 737 (N.D. Tex. 2000), *aff'd*, 254 F.3d 588 (5th Cir. 2001).

consistently has held that the goal of efficient and speedy dispute resolution must yield to the principal objective behind the passage of the Act: ensuring judicial enforcement of privately made agreements to arbitrate. *See First Options*, 514 U.S. at 947 ("[T]he basic objective [of the FAA] is not to resolve disputes in the quickest manner possible, no matter what the parties' wishes, but to ensure that commercial arbitration agreements, like other contracts, are enforced according to their terms, and according to the intentions of the parties.") (internal citations and quotations omitted). Any alleged reduction in efficiency also will flow equally from appellate arbitral review of awards, which the AAA advocates in lieu of judicial review for legal error.

Finally, although Mattel and its *amici*, particularly *amicus* United States Council for International Business, argue that allowing parties to contract for legal-error review will discourage litigants from arbitrating claims in the United States, the opposite is true. Expanded judicial review provisions – like any other provisions governing parties' agreement to arbitrate – are a matter of contract. If parties wish to forgo such review, nothing prevents them from doing so. *See* Eric Van Ginkel, *Reframing the Dilemma of Contractually Expanded Judicial Review, Arbitral Appeal vs. Vacatur*, 3 PEPP. DISP. RESOL. L.J. 157, 202-04 (2003) (stating view that parties in international arbitration will rarely use expanded review but, as with domestic arbitration, a party resisting arbitration might be amenable to such a compromise solution). Parties – such as the parties in this case – who otherwise would not arbitrate for fear of legal error by the arbitrator will be more likely to arbitrate if legal-error review from a court is available.

CONCLUSION

For these reasons and those set forth in the opening brief, the decision below should be reversed.

Respectfully submitted,

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